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UNCLAS SECTION 01 OF 03 LILONGWE 000946

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STATE FOR AF/S MELINDA TABLER-STONE
TREASURY FOR INTERNATIONAL AFFAIRS/AFRICA/BEN CUSHMAN
STATE FOR EB/IFD/ODF LINDA SPECHT
STATE PLEASE PASS TO MCC FOR KEVIN SABA
PARIS FOR D'ELIA
JOHANNESBURG FOR FCS

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SUBJECT: SUBSIDIES WORSEN MALAWI'S FOOD SHORTAGE

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LILONGWE 00000946 001.2 OF 003

SUMMARY

¶1. (SBU) In a year marked by severe shortages of food and fertilizer, it is increasingly clear that the government's interventions in these commodities have considerably deepened the crisis. The current shortage of maize is in part a result of the GOM's insistence on selling subsidized maize through its ADMARC parastatal at roughly half the import equivalent price. Fertilizer has followed a similar pattern: by announcing a heavy subsidy for all, the GOM effectively shut down private commercial sales. Both of these actions have constrained new imports. The net effect is a shortage of food five months before the next harvest, and a potentially disastrous shortage of fertilizer only weeks before planting season begins. End summary.

WHO CONTROLS MAIZE, CONTROLS MALAWI

¶2. (SBU) At the root of Malawi's chronically disrupted food and fertilizer markets is the misuse of the Agricultural Development and Marketing Corporation (ADMARC), a once-mighty agricultural monopoly. That the Banda-era institution survives to this day is proof of Malawian policymakers' addiction to popular subsidies, an almost willful ignorance of how markets work, and an abiding distrust of the private sector. In essence, ADMARC has been used as a state tool in trying--and consistently failing--to maintain a command economy in the dominant agricultural commodity and food staple: maize.

¶3. (SBU) Since last year, the GOM has kept ADMARC's retail price for maize at MK17/kg ($0.14/kg) as the commercial price has reached double that. As the impending shortage became apparent, the GOM began making plans for large commercial imports of maize on the order of 100,000 metric tons (MT) even as it was asking "donor countries" to

mobilize a major effort for humanitarian relief. The diplomatic and development missions pushed back, asking Malawi to limit its commercial imports and instead allocate money for humanitarian relief. It has done that to some extent, essentially splitting its purchases between humanitarian and commercial purposes.

POOR SIGNALING COMPLICATES THE PROBLEM

¶4. (SBU) Still, the government failed to settle firmly on the size and nature of its commercial intervention, much less communicate that intention to the marketplace, leaving private-sector buyers to assume the worst. Thus, as happened in the food crisis of 2001/02, consumers have avoided paying the higher prices offered by private traders. These, in turn, have had little revenue, and less forward price incentive, to finance imports. The same signal has discouraged large farmers from growing maize commercially, which they tell us would happen if the retail price floor reached the MK20-26 ($0.16-21) price range (i.e., an increase between 20 and 50 percent). Meanwhile, the landed cost of imported maize has risen as regional stocks have declined and transport prices have increased.

¶5. (SBU) This situation was expensive for the GOM but stable until ADMARC stocks predictably began to run out. At this writing, the exhaustion of cheap ADMARC stocks is creating a panic that "there is no maize" in many trading centers, when in fact there are at least some private stocks, available for higher prices (MK28-36/kg)($0.23-29). At the urging of foreign development missions, the Cabinet approved a "cost recovery" price of MK22-24/kg ($0.18-20) (still subsidized,

since actual cost recovery would be MK28-32/kg), but has so far failed to communicate the change formally to ADMARC. With the GOM struggling against impeachment in Parliament, it is very unlikely to do so, though this modest change could still stimulate private imports. The most likely result will be sharp price spikes on the private side as ADMARC stocks run out, and more people will spill over into the humanitarian relief pool. (At the grassroots level, the high price and scarcity of maize have stimulated an increase in winter cropping, which could ameliorate the crisis in some areas. Unfortunately, the GOM does not measure winter crops well, so the effect is unpredictable at this point.)

GOVERNMENT TAKES FERTILIZER BACK

¶6. (SBU) The fertilizer market has suffered from much the same pattern of intervention from the GOM, though on a less spectacular scale. The market had made considerable progress in liberalizing and building a private distribution network until this year. Last year, the private sector imported roughly 95 percent of total fertilizer imports. But the GOM, still feeling the sting from having bungled last year's targeted free fertilizer scheme, determined to do things itself this year. It has settled on roughly a 50 percent subsidy on some 135,000 MT of fertilizer, including some 70,000 MT of its own imports. (The country's total demand is about 220,000 MT.) Contributing its two cents to the debate, the main opposition party has demanded a universal subsidy, so as to cover its political base of tobacco farmers.

¶7. (SBU) As if displacing about 1/3 of the market weren't bad enough, the GOM was late solidifying its plans and bad at communicating what those plans were. So, around July,

commercial fertilizer sales came to a standstill as buyers waited to see what the subsidy scheme would be. Since most fertilizer companies are thinly capitalized, they have been unable to order the quantities of fertilizer they think will be needed before the November-December planting season. Fertilizer that would normally have been ordered, shipped, and distributed by August-September has yet to be ordered, and it is now practically too late.

COMMENT: BAD POLITICS, WORSE INSTINCTS

¶8. (SBU) The Mutharika administration came into office on a platform of fiscal responsibility and economic reform, and it has performed reasonably well in general. But where it comes to maize and the intensive agricultural inputs needed to grow maize, it has clung to the old state-centric way of doing things. At the political level, Mutharika's weakness in Parliament has made it necessary buy off the opposition with deeper and broader fertilizer subsidies than it wants. With half the Parliament crying for impeachment, the increasingly gross subsidies on maize have become untouchable.

¶9. (SBU) Perhaps in perfect politics-free vacuum, the Mutharika administration may have continued the nascent liberalization of the agriculture markets. But even among the economic liberals in the government, it is not clear that free-market ideas can win over cultural instinct when it comes to food. Malawians of the political class still distrust "traders" (a term generally preceded in the local press by "unscrupulous" and often by "Asian"), and they tend to blame them for any market failure. (2001/02 is viewed by many otherwise free-marketers as the year the private sector let Malawi down.) In a lean year, these instincts are exaggerated, and the state is driven to try to control the markets further, deepening the failure. That is happening now, and there is next to no chance of breaking free until next year. If history provides any pattern, this year's disaster will somehow be blamed on

unscrupulous traders, and the government may cling even tighter to its command-economy approach to food.
EASTHAM